

periodically advanced with respect to an issue, the date of issue is when the first of such obligations under the issue is created and the funds are advanced.

(2) The term *maturity* means those obligations of the issue having both the same maturity date and the same stated interest rate.

(3) The term *term of an issue* means the duration of the period beginning on the date of issue and ending on the latest maturity date of any obligation of the issue without regard to optional redemption dates.

(4) The term *lendable proceeds* means the amount of the original proceeds, net of amounts allocated to a reasonably required reserve or replacement fund. See generally § 1.103-13(b) and § 1.103-14(d) for further definitions.

(5) The term *initial principal user* means each person who as of the date of issue is obligated to use the facility to such an extent that under section 103(b)(6) such person would be treated as a principal user. With respect to organizations described in section 501(c)(3), however, such determination is made without regard to whether such organization is treated as an exempt organization under section 103(b)(3) and § 1.103-7(b)(2).

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**§ 5f.163-1 Denial of interest deduction on certain obligations issued after December 31, 1982, unless issued in registered form.**

(a) *Denial of deduction generally.* Interest paid or accrued on a registration-required obligation (as defined in paragraph (b) of this section) shall not be allowed as a deduction under section 163 or any other provision of law unless such obligation is issued in registered form (as defined in § 5f.103-1(c)).

(b) *Registration-required obligation.* For purposes of this section, the term “registration-required obligation” means any obligation except any one of the following:

(1) An obligation issued by a natural person.

(2) An obligation not of a type offered to the public. The determination as to whether an obligation is not of a type offered to the public shall be based on

whether similar obligations are in fact publicly offered or traded.

(3) An obligation that has a maturity at the date of issue of not more than 1 year.

(4) An obligation issued before January 1, 1983. An obligation first issued before January 1, 1983, shall not be considered to have been issued on or after such date merely as a result of the existence of a right on the part of the holder of such obligation to convert such obligation from registered form into bearer form, or as a result of the exercise of such a right.

(5) An obligation described in subparagraph (1) of paragraph (c) (relating to certain obligations issued to foreign persons).

(c) [Reserved]

(d) *Effective date.* The provisions of this section shall apply to obligations issued after December 31, 1982, unless issued on an exercise of a warrant for the conversion of a convertible obligation if such warrant or obligation was offered or sold outside the United States without registration under the Securities Act of 1933 and was issued before August 10, 1982.

(e) *Obligations first issued after December 31, 1982, where the right exists for the holder to convert such obligation from registered form into bearer form.* [Reserved]

(f) *Examples.* The application of this section may be illustrated by the following examples:

*Example (1).* All of the shares of Corporation X are owned by two individuals, A and B. X desires to sell all of its assets to Corporation Y, all of the shares of which are owned by individual C. Following the sale, Corporation X will be completely liquidated. As partial consideration for the Corporation X assets, Corporation Y delivers a promissory note to X, secured by a security interest and mortgage on the acquired assets. The note given by Y to X is not of a type offered to the public.

*Example (2).* Corporation Z has a credit agreement with Bank M pursuant to which Corporation Z may borrow amounts not exceeding \$10X upon delivery of Z's note to Bank M. The note Z delivers to M is not of a type offered to the public.

*Example (3).* Individuals D and E operate a retail business through partnership DE. D wishes to loan partnership DE \$5X. DE's note evidencing the loan from D is not of a type offered to the public.

*Example (4).* Individual F owns one-third of the shares of Corporation W. F makes a cash advance to W. W's note evidencing F's cash advance is not of a type offered to the public.

*Example (5).* Closely-held Corporation R places its convertible debentures with 30 individuals who are United States persons. The offering is not required to be registered under the Securities Act of 1933. Similar debentures are publicly offered and traded. The obligations are not considered of a type not offered to the public.

*Example (6).* In 1980, Corporation V issued its bonds due in 1986 through an offering registered with the Securities and Exchange Commission. Although the bonds were initially issued in registered form, the terms of the bonds permit a holder, at his option, to convert a bond into bearer form at any time prior to maturity. Similarly, a person who holds a bond in bearer form may, at any time, have the bond converted into registered form.

(i) Assume G bought one of Corporation V's bonds upon the original issuance in 1980. In 1983, G requests that V convert the bond into bearer form. Except for the change from registered to bearer form, the terms of the bond are unchanged. The bond held by G is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

(ii) Assume H buys one of Corporation V's bonds in the secondary market in 1983. The bond H receives is in registered form, but H requests that V convert the obligation into bearer form. There is no other change in the terms of the instrument. The bond held by H is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

(iii) Assume the same facts as in (ii) except that in 1984 I purchases H's V Corporation bond, which is in bearer form. I requests V to convert the bond into registered form. There is no other change in the terms of the instrument. In 1985, I requests V to convert the bond back into bearer form. Again, there is no other change in the terms of the instrument. The bond purchased by I is not considered issued after December 31, 1982, under § 5f.163-1(b)(4).

*Example (7).* Corporation U wishes to make a public offering of its debentures to United States persons. U issues a master note to Bank N. The terms of the note require that any person who acquires an interest in the note must have such interest reflected in a book entry. Bank N offers for sale interests in the Corporation U note. Ownership interests in the note are reflected on the books of Bank N. Corporation U's debenture is considered issued in registered form.

*Example (8).* Issuer S wishes to make a public offering of its debt obligations to United States persons. The obligations will have a maturity in excess of one year. On November 1, 1982, the closing on the debt offering occurs. At the closing, the net cash proceeds of

the offering are delivered to S, and S delivers a master note to the underwriter of the offering. On January 2, 1983, S delivers the debt obligations to the purchasers in definitive form and the master note is cancelled. The obligations are not registration-required because they are considered issued before January 1, 1983.

*Example (9).* In July 1983, Corporation T sells an issue of debt obligations maturing in 1985 to the public in the United States. Three of the obligations of the issue are issued to J in bearer form. The balance of the obligations of the issue are issued in registered form. The terms of the registered and bearer obligations are identical. The obligations issued to J are of a type offered to the public and are registration-required obligations. Since the three obligations are issued in bearer form, T is subject to the tax imposed under section 4701 with respect to the three bearer obligations. In addition, interest paid or accrued on the three bearer obligations is not deductible by T. Moreover, since the issuance of the three bearer obligations is subject to tax under section 4701, J is not prohibited from deducting losses on the obligations under section 165(j) or from treating gain on the obligations as capital gain under section 1232(d). The balance of the obligations in the issue do not give rise to liability for the tax under section 4701, and the deductibility of interest on such obligations is not affected by section 163(f).

*Example (10).* Broker K acquires a bond issued in 1980 by the United States Treasury through the Bureau of Public Debt. Broker K sells interests in the bond to the public after December 31, 1982. A purchaser may acquire an interest in any interest payment falling due under the bond or an interest in the principal of the bond. The bond is held by Custodian L for the benefit of the persons acquiring these interests. On receipt of interest and principal payments under the bond, Custodian L transfers the amount received to the person whose ownership interest corresponds to the bond component giving rise to the payment. Under section 1232B, each bond component is treated as an obligation issued with original issue discount equal to the excess of the stated redemption price at maturity over the purchase price of the bond component. The interests sold by K are obligations of a type offered to the public. Further, the interests are, in accordance with section 1232B, considered issued after December 31, 1982. Accordingly, the interests are registration-required obligations under § 5f.163-1(b).

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